

Sept. 5, 1990

LETTER 1051

QUESTION: President Bush has changed his goal. Where first he wanted to rid the world of Hussein, he will now settle for Iraq pulling out of Kuwait.

All right, what happens if Hussein agrees to pull out of Kuwait? As matters stand, Hussein now possesses Kuwait's gold and assets, and he's raped and pillaged the land. But if Hussein pulls back, he'll still represent the same threat. The US military will still be stuck, sweltering in the fierce heat of the Middle East, guarding Saudi Arabia. The excitement will be over. The home folk and the soldiers will first become disenchanted, then impatient, then exasperated. The huge expenses of the operation will continue to mount. Then what?

COMPOUNDING DEBTS: People are under the illusion that the confrontation with Saddam Hussein is the reason for this bear market. Nothing could be further from the truth. The basic reason for this primary bear market is that the US has borrowed and spent itself to the point where its currency, the dollar, and a good portion of its economy, are beginning to look bankrupt.

For years I've warned about the twin dangers of ever-rising deficits and compounding debt. Those dangers have loomed ever-larger and now they have assumed the form of an economic Frankenstein monster.

It was one of the French Rothschilds who said that he was very familiar with the Seven Wonders of the World -- but he knew of an eighth. When asked what the eighth was, he stated simply, "Compound interest."

Compounding your assets will make you rich. But few people really understand the dangers of compounding your debts. Here's a good example. Interest on the US federal debt for the single month of July was \$18.4 billion. So far this fiscal year, interest on the debt is \$228.6 billion. And are you ready for this --for the current full fiscal year (which ends October 1) the interest on the debt is projected to be \$261.1 or \$4.06 billion a week. The US government is being eaten alive by debts and deficits and the compounding interest on those debts and deficits. Is it any wonder that the dollar has been in a free fall?!

I've been writing until I'm blue in the face about this literally criminal increase of US debts and deficits. Balancing the US budget has become an impossibility. I can't emphasize enough the size of the coming disaster to the dollar, to bonds, to stocks and to the US economy, as these debts continue to snowball totally, tragically, idiotically out of control.

The Iraq mess has compounded the compounding problem. And because of the Iraqi situation, we are hearing and reading columns such as the one below (from *USA Today*, August 24).

This is wrong time to worry about deficit

BETHESDA, Md. — A tax hike now would drain the last bit of blood from our anemic economy — and it might even jeopardize our efforts in the Persian Gulf.

We are dangerously close to an economic recession. Rising oil prices brought on by Iraq's invasion of Kuwait and the ensuing

Aug. 24 DJIA 2532.92; PTI 3231; A-D Ratio -15.13
Aug. 30 DJIA 2593.32; PTI 3231; A-D Ratio -14.48
Dow Yield: 4.13%; Dow P/E: 12.6; DowPow: -506
Dow Book Value: 1276; Dow 200-day MA: 2745
Percentage of Undervalued Blue-chips: 25%
PTI 89-day Moving Average: 3263

Question: What are the possible outcomes of the current debt/deficit trend?

Answer: We're seeing some of them now -- a crashing dollar, a battered stock market, battered bonds and an economy sliding into recession or worse.

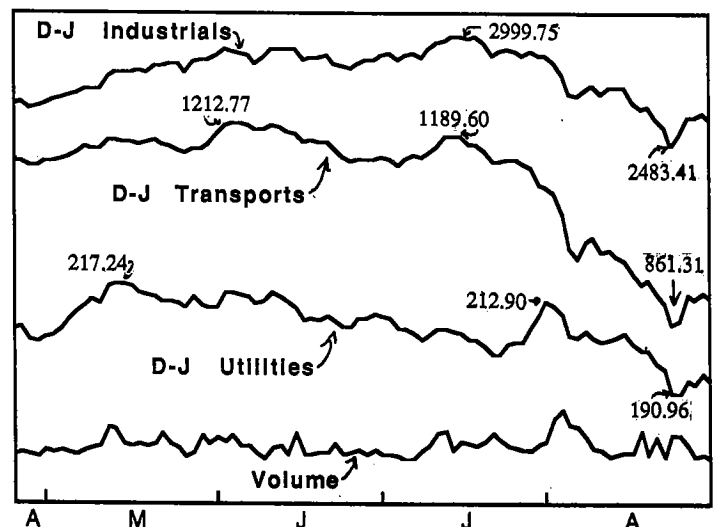
Question: No, I mean how do you think the debt problem can be resolved?

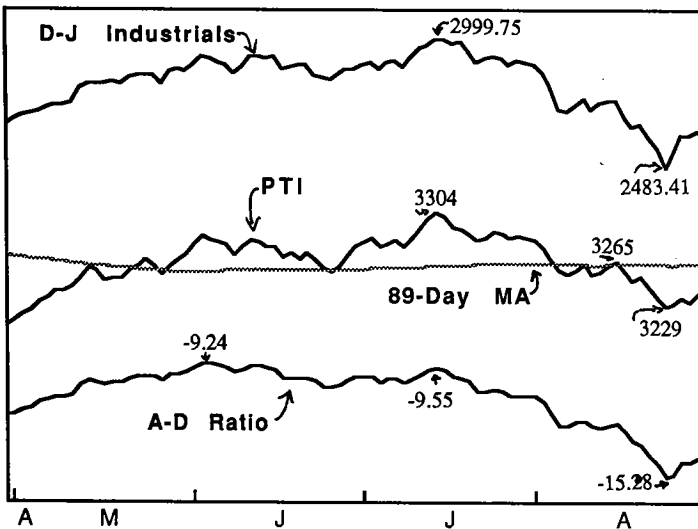
Answer: Very painfully. At some point the US might announce that it will not redeem long or even intermediate-term Treasury debt -- it would only pay the interest on the debt as it comes due. If that were to happen, it would mean that holders of T-bonds would be locked into perpetual-maturity bonds.

Another possibility would be runaway inflation, inflation that would destroy the value of the dollar and thus wipe out the dollar debt. But if this were to occur, the bond markets would collapse (haven't they been doing that?), interest rates would go through the roof, and this nation would plunge into a deflationary depression.

A third possibility would be a moratorium on debt payment while Congress tried to figure out an emergency plan to re-schedule or re-finance the debt. I don't know how this might work, but it would create an all-out panic to get out of bonds.

A fourth possibility would be for the US to mandate a balanced budget by law -- and then take the depression that this would bring on (through a collapse in government spending), and a policy of running surpluses in the federal budget. In other words, the US would move to actually pare down the federal debt. The problem here is that the tax receipts to the Treasury would collapse during a recession/depression (they are doing that now), and with tax receipts collapsing, this would render the federal deficits worse than ever.





Question: But what about Gramm-Rudman?

Answer: I fully expect that Congress will change the Gramm-Rudman law because of the new military emergency. Any serious cutting of the budget will be put off into the late-1990s. And if a recession starts, the sequestering demands of Gramm-Rudman are automatically suspended.

Conclusion: At this point I don't have any brilliant concept for solving the budget crisis. And if I did, I can guarantee that Washington wouldn't be interested. I can only say what I think is actually happening -- what I think is happening is that the finances of the US government are beginning to unravel.

THE PICTURE: This is a tough letter to write -- tough because we're in such a news-oriented market. A news-driven market is one that can turn on a dime, depending on what comes out over the TV or radio at any given minute. Also, this is a market that has been oversold since early July (a bear market can stay oversold for months at a time). But when a market is this oversold, when a market is this compressed, any good news can send it spiraling upward in an explosive bear market (upside) correction.

By August 23, we were witnessing markets that were literally "blowing off" on the downside. Stocks, bonds, the dollar, the various averages -- all were in states of extreme downside compression. In the space of a few months, many stocks had literally crashed. Analysts who had been bullish right up to late-August suddenly jumped to the bear side. Put buying and short selling became too easy, too popular. On Friday, in a day dominated mostly by Dow stock buying, the Dow surged. Last Monday (Aug. 27), the rally gathered steam with the Dow up 78 points and breadth heavily to the upside.

The market is now heavily oversold, more so than at any time in recent years. This is a bear market, however, and in bear markets oversolds can become more oversold, and corrective advances can start at any time.

As this is written, it is impossible to say whether we have seen an important secondary bottom in this bear market or whether the stock market will have to undergo one more downward sweep in order to render a thoroughly sold out condition and a solid secondary bottom.

This is a market filled with irony. Consider this -- under Dow Theory a primary bear market started on September 5, 1989. That was the day when the D-J Industrials and Transports recorded their last confirmed highs together. The advance-decline ratio had topped out a few days earlier, on September 1 (and the A-D has been going down ever since).

Four months after the top, on January 25, 1990, the Dow Theory signaled that a primary bear market was in force. Market conditions continued to deteriorate throughout 1990. But strangely, nobody really got excited until Iraq-Kuwait hit the headlines.

Hussein's invasion gave people a "real" reason to sell. The takeover of Kuwait was something tangible -- far more visible than say declines outnumbering advances day after day or the dollar smashing to embarrassing new lows.

But as I said in the last Letter, from the standpoint of the bear market, all the Iraqi mess is going to do is extend the life of the bear. The Iraqi invasion didn't trigger the bear market and the Iraqi invasion won't end it.

This bear market is about debts, deficits, deceit, corruption, over-speculation, and excesses -- excesses built into the economy and the stock market ever since the bull market began back in 1974. This bear market is about a slumping dollar, interest rates that are rising in the face of recession, global competition and politicians who put self-election before anything else -- and I mean literally anything.

In the last Letter I gave some potential targets for the bear, and they run something like this. If the Dow gets down to the point where it yields 6% (which is not uncommon in a major bear market), then the Dow will ultimately sell in the mid-1700s. But if dividends are cut as the bear market progresses, then the Dow could even sell below 1700.

Again, if the bear market corrects just half of the gains of the preceding bull market (and most bear markets erase more than half the preceding bull market's gains), then the Dow could decline to the mid-1700s.

These are just theoretical levels, and it might be more honest and more accurate to simply fall back on the Dow Theory rule that states, "Neither the duration or the extent of a primary movement can be forecast beforehand." Which is another way of saying that the market is a law unto itself, and it will go where it wants in its own good time.

PHASES: Every bear market is divided into three psychological phases (not to be confused with price movements). The first phase (already passed) is the one in which stocks sell off as they eliminate the foam and froth of the preceding bull market top.

I believe this phase ended around the time of the Iraq incursion. Up to that time, even though the market breadth had been going down for months, there was still talk of "Dow 3500" and people really didn't accept the idea that a bear market had started.

I don't remember any second phase of a bear market beginning with a news event, but there's always a first, and I do feel that the second phase of this bear market started a few weeks ago when Hussein invaded Kuwait.

The second phase is the one in which stocks go down as they reflect obviously deteriorating business conditions and falling corporate profits. There is no doubt but that is what's happening now. The second phase is usually the longest and most deceptive phase of a bear market. Typically in the second phase we see panics in the market and collapses in individual stocks as shockingly poor earnings are released. We also see sudden and violent (upward) corrections. I might add that it is characteristic for cries of "new bull market" to greet each of these deceptive bear market rallies.

Finally, the third phase will arrive. This is the liquidation phase, the phase where good stocks are thrown in with the bad -- for whatever price they might bring. In the third phase, people have to raise money, and stocks in this phase may drop far below known values.

As I said, we are now in the second phase of the bear market. Stocks here can be expected to react very adversely to bad news. Panic action can be expected to appear at any time. Violent rallies are also a characteristic of the second phase. The second phase can be a long one, lasting a year or two or even longer.

SUPPORT LEVELS: As this bear market makes its way irregularly to lower levels, we will hear a lot about downside support levels. Pay no attention to such talk -- it's mostly from neophyte analysts who have little or no experience with bear markets.

During primary movements (either bull or bear) it is usual for the Averages to show little respect for previous so-called important levels. During a primary bull market, the Averages will cut right through previous "resistance" levels as though they didn't exist. Conversely, in a primary bear market, the Averages will slice through previous "support" levels like a hot knife cutting through margarine (I don't use butter).

So the above concept is important to remember. And next time your market guru tells you, "The Dow will support and then rally off the 2400 level, just smile and tell him 'thanks for the valuable information'."

THE US VIEW: The US view is the narrow view in today's global world. Each week I receive a large number of foreign publications -- everything from the London *Economist* to British and German advisory publications to Swiss bank reports to Canadian brokerage house advisories. I feel it's absolutely necessary these days to have the international view. But it's a perspective that the great majority of American investors don't have.

The international view, judging from what I read, is that the US deficits are chronic with no let-up in sight. And with the arrival of a US recession, tax receipts to the Treasury are falling off, rendering the deficit picture worse than ever. The straw that broke the dollar's back was Iraq and all the expenses connected with the current huge military build-up.

I don't know how the US is going to solve its deficit problem. I thought I knew ten years ago, but at this point, with the compounding of over \$3 trillion in federal debt (and more debt being added every day), the solution is beyond me. It's a self-perpetuating, ever-compounding, out-of-control monster.

The IMF has forced austerity on various profligate member nations that have applied for loans. At some point will austerity be forced on the US via our creditors? If that happens, the US will lapse into a severe depression, and nobody wants that to happen (although we may be heading for one anyway, regardless of what people want).

Of course, another temporary "solution" would be to follow the example of Canada, Australia and Britain -- that is, to run interest rates up so high that the dollar becomes irresistibly attractive. If the Fed follows that route (and it would occur within the context of a primary bear market), you'll see stocks hit lows that you won't believe. That in turn would set off major bankruptcies and probably a depression.

The way in which the US has handled its debts in the past was to inflate them away. But that method won't work any longer, not with the dollar being the world's reserve currency and not with the US being the world's biggest debtor.

So there's no way out of this debt/deficit disaster which doesn't entail severe pain. That's the crux of it. If any reader knows of any way to get out of our debt debacle in a painless way, please -- let me know about it.

But make no mistake about it -- these same thoughts must be going through the minds of the creditors who hold our bonds. Yes, our

creditors must be wondering (as the dollar sinks lower week after week) how much longer they can afford to hold US debt.

CIRCUIT BREAKERS: I've been asked what I think about the so-called "circuit breakers" on the NYSE. As far as I'm concerned, circuit breakers are strictly for public relations. Anything that halts trading on the exchange for any reason whatsoever simply interferes with liquidity. What's the difference whether the market goes up or down 250 points in two days without circuit breakers or in two weeks with circuit breakers? The market is going to the same place -- it's just a matter of whether it goes there freely or with interference from the authorities on the exchange.

Of course, program trading adds tremendously to market volatility, and as far as I'm concerned, I'd be happy to see them ban this form of guaranteed profit speculation on the part of the institutions and brokerage houses. But the exchange needs the volume, and the brokers need the commissions, so this won't happen any time soon.

INFLATION: Lacey Hunt is one of the economists that I respect. In an interview on FNN last week, Hunt stated that he felt that the inflation rate would rise to 8% this year if the oil situation remained pretty much as it is now. The normal rate on long-term T-bonds is about 3% over the inflation rate. If that's true, look for long rates over 11% before the year is out. And of course, that doesn't take into consideration the budget mess, which, I feel, will drive long rates up no matter what occurs with oil.

INVESTMENT POSITION: My instinct here is to tell you that it's time to sit tight. The market looks like it may want to correct (on the upside) here, so if you haven't sold, it may be that there'll be a better time to sell coming up.



I still don't feel that kind of black "I hate the stock market" pessimism that I would like as far as identifying even a secondary bottom, but I feel it's about a 50/50 chance that we've formed our first secondary bottom.

Subscribers should remember that this is a primary bear market, and I very seldom advise buying stocks "to beat the bear." So if you are thinking of "doing a little trading," you're on your own -- I didn't tell you to do it.

Everything's been hammered down pretty well, and that even includes bonds, so we could have some upside action in the bond area as well.

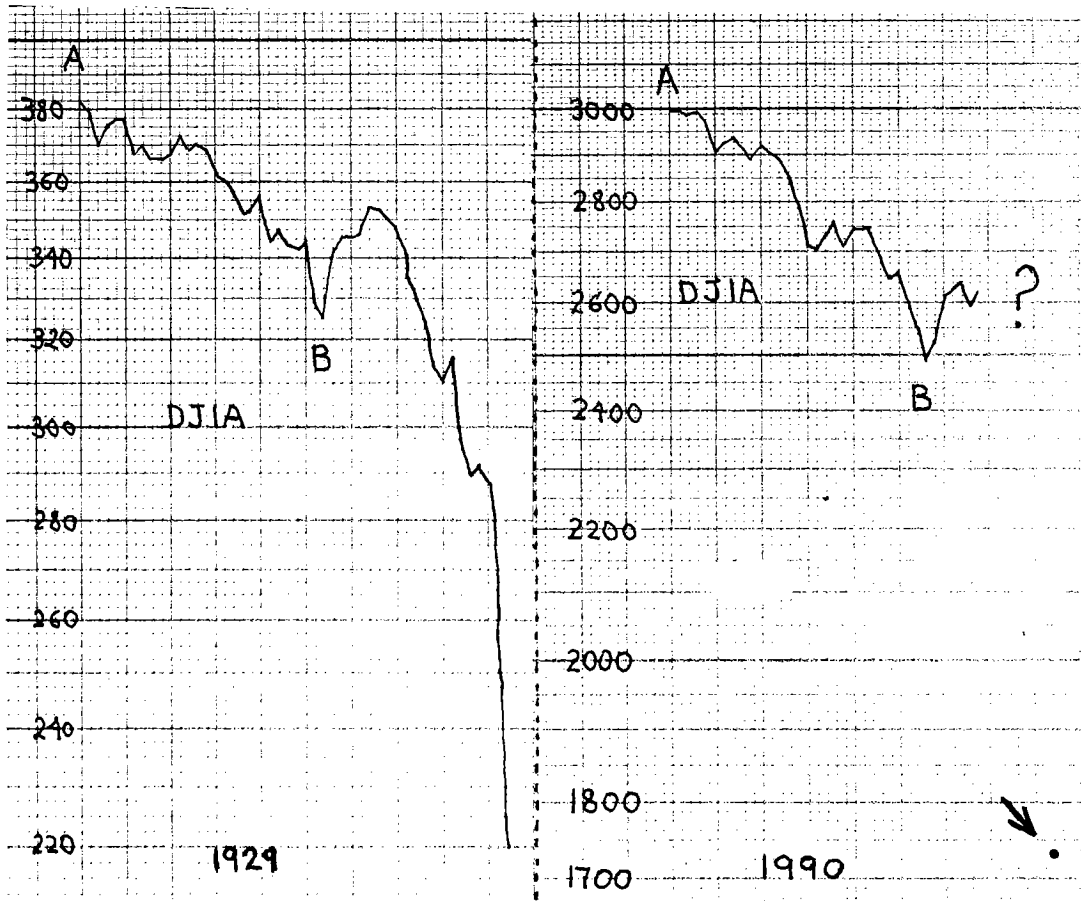
However, I continue to feel that the fundamentals for the dollar are so rotten that I can't get enthusiastic about interest rates coming down or bonds going up.

Personally, I'm sitting tight with some T-bills, some German marks and Swiss francs and my gold coins. I'm not eager to garner profits when the bear is in the box -- what I basically would like to do is avoid losses.

In the past I've reminded subscribers, "In a true primary bear market, the person who loses the least is the winner."

Subscribers wishing to purchase foreign currencies may call Mr. Frank Trotter of the Mark Twain Bank of St. Louis, Missouri -- (800) 926-4922. This bank will buy you CDs in any currency, and accounts are insured by the FDIC up to \$100,000. The bank requires a minimum of \$10,000 for foreign CDs.

1929 and NOW: My old friend, Joe Granville, is an originator. While we're sleeping, Joe is thinking. Now he's come up with the concept that there are remarkable similarities between the crash off the September 3, 1929, peak and the smash of 1990. Joe outlined



all the daily Dow statistics from September 3, 1929, to the first crash bottom on October 29, 1929. That crash-action took the Dow from 381.17 down to 220.07, a dreadful drop of 42%.

Against that, Joe showed the Dow statistics, starting with July 16, 1990, and projecting (based on 1929 percentages) to September 20, 1990. If today's market were to follow 1929 exactly, the Dow would be 1732 on September 20, 1990.

I charted the action of the two periods on ratio chart paper so that the two periods can be compared accurately (the movements are shown on the charts in percentages).

Note how remarkably similar the two periods are -- SO FAR. The decline from A to B in 1929 resulted in a loss of 14.6%. The decline from A to B in 1990 was even greater at 17.2%. If 1990 were to follow the 1929 pattern, then when the current rally is over the Dow would have to crash down to 1732 -- and this within the period around the end of September (the arrow and the dot show where the Dow would have to be to duplicate the 1929 pattern).

Can it happen? Can today's market duplicate the unbelievable pattern of 1929? The old adage states, "The market can do anything."

But will it happen? The odds are always against history repeating exactly. But let's wait and see (*The Granville Market Letter*, PO Drawer 413006, Kansas City, MO 64141).

TRAVEL: My wife Faye is off for three weeks in France. She's taking two bike trips, one through Provence and one through Burgundy. I was going to go with her, but I chickened out because I really dislike traveling so much. I like being there, but it's the actual traveling that drives me up the wall.

Two weeks ago we went to San Francisco where I spoke at the fine ISI Conference. It took five hours to go from our house in La Jolla

to the Fairmont in SF. Our plane was half an hour late coming in, and then it was grounded for another half hour because of fog and crowded conditions in San Francisco. Then the taxi ride from SF to the city took over an hour because cars were dragging along bumper-to-bumper from the airport. Ten years ago I could have gone from San Diego to New York in almost the same time.

I feel that traveling has become an imposition, and for the most part a nasty experience. Now don't get me wrong, I love Paris. If you could just transport me there in a few hours, I'd be there with Faye. But my feeling is that if I can avoid torture, I will. And travel, in my opinion, is torture today (P.S. I won't even go into the problem of what the Yankee dollar will buy in Europe or the Far East today). Or to put it another way, if you're going shopping, do it in the USA -- your dollar isn't worth that much anywhere else -- except in third world countries.

GIMMICKS: Everybody loves a stock market gimmick, better known as a crystal ball. With literally millions of people trying to dig out the secrets of the stock market, there are obviously going to be a lot of people searching for matching series.

One of the best known matching series is the so-called Super Bowl series in which it is stated that if an NFC team wins the Super Bowl the market will be up that year and conversely if an AFC team wins the market will be down. The series has worked quite well, but here's the real story. Every set of coincidences can last just so long, and it's very much like flipping two coins. They may land heads five times and tails ten times, at which point you can say that if the first coin lands heads the second coin is almost sure to land heads too -- based on the amazing past series. But my advice is -- don't bet on it. And don't bet on the Super Bowl series.

Then there is the hemline theory, based on the premise that the market will go up or down with the hemline of women's skirts.

A remarkable set of coincidences was put forth by Thomas Meyers of West Trenton, NJ. He shows where the annual direction of the

Direction of Stock Prices

Year	Direction	Year	Direction
1915	Up	1976	Up
1916	Down	1977	Down
1917	Down	1978	Down
1918	Up	1979	Up
1919	Up	1980	Up
1920	Down	1981	Down
1921	Up	1982	Up
1922	Up	1983	Up
1923	Down	1984	Down
1924	Up	1985	Up
1925	Up	1986	Up
1926	Up	1987	Up
1927	Up	1988	Up
1928	Up	1989	Up
1929	Down	1990	?
1930	Down	1991	?
1931	Down	1992	?
1932	Down	1993	?

stock market from 1976 to 1989 corresponded with the annual direction of the stock market from 1915 to 1928. Here is the series as published by *Investor's Digest* of Ft. Lauderdale, Fla.

Since 1929 through 1932 were down years, Mr. Meyers hazards that 1990 through 1993 will also be down years. It may work out that way (after all, we are in a bear market), but I wouldn't bet on it.

The sad fact is that there is no easy or gimmicky method of predicting the direction of the stock market. I've searched for 45 years myself, trying to find the perfect solution to "what the stock market will do this year and next," and I'll confess that if there is an answer, it's eluded me.

The nearest thing to a solution to the problem is probably the oldest one, and it's the one defined by Dow Theory. The solution goes like this -- once a bull market starts it goes to conclusion (low yields, few values, high speculative sentiment, brokerage house excitement, etc.). The bull market ultimately gives way to a bear market, and once the bear market starts it goes to its ultimate conclusion (fat yields, great values, gloom, doom, scandals, liquidations).

So that's it -- bull markets come and go, and they are followed by bear markets that come and go, and all our efforts, all our money, all our studies, all our gimmicks, don't change that progression.

Therefore, most of my work has to do with identification rather than prediction. If I can identify a bear market, I can predict that stocks will go lower and finally reach a level of undervaluation. The converse is true if I can identify a bull market. So forget the gimmicks, forget the computer-generated forecasting tools, forget Super Bowls and hemlines and matching series. In the end, they don't work when you need them most. And in the majority of cases, they'll cost you money.

After all, when a few serious investors spend the better part of their working day studying values and major trends and in doing so, make a living, why should you, with a knowledge of ladies' hemlines, be able to beat the market?

NOTES & QUOTES: Various commentators are saying, "After Iraq, the world will never be the same." I'm not convinced. As far as the stock market is concerned, I'm more inclined to view Iraq as a cover-up for what's actually happening, at least in the US (the Iraqi situation will eventually be solved, but the US debt situation is not going to go away).

The fact is that the US has been on notice for years that it is far too dependent on Mideast oil. We did nothing about it. There's no strategy coming out of Washington, no long-term plans -- in energy, in education, in pollution, in immigration, on the budget. Washington simply reacts to the crisis of the month or the crisis of the year. I've said it before, and I'll repeat it -- Reagan was lucky. And Bush has been lucky -- up to now.

Japan may have been lucky too -- up to now. At its recent low, the Nikkei stock average had lost 37% of its peak value. In *Barron's* (August 27), Asian expert Mark Faber states that he believes a bear market is in force in Japan, a bear market that will not end until 1992 or 1993. Says Faber, "I think the Japanese shares could again yield 2.5%, and that implies an index of anywhere between 10,000 and 15,000." The high for the Nikkei was 38,957, December 1989.

In a second article, *Barron's* notes that Japan's 92 million acres of land are priced at a fantastic \$11 trillion. Probably half the loan portfolios of all the Japanese banks are, in one form or another, collateralized by Japanese real estate (Japanese banking and real estate stock prices have already dropped an average of 60%).

The Sept. 3 issue of *Insight* magazine notes that the average price for a home in Tokyo is \$432,000 and the average size of that home is 674 square feet. Furthermore, 55% of Tokyo's workers travel more than two hours to and from work and 20% of the workers travel more than four hours each day. The six-day work week is still common in Japan.

Maybe it's starting. Voters in the state of Colorado will have a chance in the coming election to decide whether they want to LIMIT the terms of state and federal politicians. I've long advocated limiting political terms, and maybe, just maybe, this is the beginning. I consider American political dynasties to be one of the basic reasons for the outrageous growth of debt in the US. The biggest thing in a politician's life is getting elected, and re-elected and re-elected. Therefore, the pols compete with each other to vote in spending programs which they think will buy them votes. We'll never end the deficits until either (1) we face a credit disaster or (2) we limit the terms of the politicians (and I'm afraid we face number one now).

Moody's Investors Service announced that junk bond defaults in 1990 so far are the highest in 19 years.

GM is asking NY car dealers to shell out big bucks for the privilege of selling Saturn, their new car. Dealers are expected to spend \$2-4 million for the franchises. GM hopes that each dealer will sell as many as 1,000 Saturns per year. Mmmm.

The tally on 26,000 owner complaints about car problems is in. This is a listing of the cars with the FEWEST complaints. Only one US car made the top 10, and that was Buick. But can you believe that Buick took out full page ads in national magazines boasting that they came in fifth? Is that what the US automobile industry has come to?

In the meantime Chrysler has been fined \$7.6 million for selling 30 previously wrecked cars as new cars, for disconnecting the odometers on 60,000 new cars driven between one day and five weeks by Chrysler executives and for changing odometers on cars which had been left connected.

Ruble contract, or what will they trade next? Coming up, you will very probably be able to buy futures on the ruble (one of the major exchanges is trying to get a ruble contract approved). Of course, whether rubles will ever be worth anything is anybody's guess. Right now the ruble is a bankrupt currency, but it's always possible that the Soviets will get sensible and make the ruble convertible into gold.

By the way, the Soviets have just announced that they are making plans for facilities to convert the ruble into hard currencies. That may prove embarrassing, because if they do it the world will then see how little the ruble is worth.

Hotel prices making you angry? Join the club. My own feeling is that in the new world of the 1990s expensive hotels are going to take a beating, and that NYC's Ian Schrager is very probably on to the wave of the future. Schrager has been converting beat-up old hotels to beautiful, advanced-design show places. If you're in NYC visit the Royalton on West 46th Street or the new Paramount (with rooms starting at \$99). "Less costly, well designed hotels are an idea whose time has come," says Schrager. "It's happened in the clothing industry with the Gap, it's happening in restaurants. It's cheap chic." Russell comment: I agree 100%. I've been saying for a few years that the US' massive debt will produce lowered standards of living. Schrager's idea is to keep the standards up -- but the costs down. It's the wave of the future -- in all services.

The real estate slump is hitting NYC hard, according to the August 20 *New York Times*. Says a front page article, "Some of New York's wealthiest and best-known developers, squeezed by the region's economic retrenchment and a dearth of young, high-salaried professionals, have missed monthly mortgage payments on large apartment complexes and, in at least one case, defaulted on a \$100 million mortgage."

Trading options: I've never recommended it. Jim Donahue, who ran *Hedged Securities Associates'* limited partnerships announced last week that he lost \$100 million in trading, thus wiping out all his limited partners. He was so mortified by his losses that he sent the 1,000 limited partners the sad story on a videotape.

Financial Adviser Gives Videotaped Confession

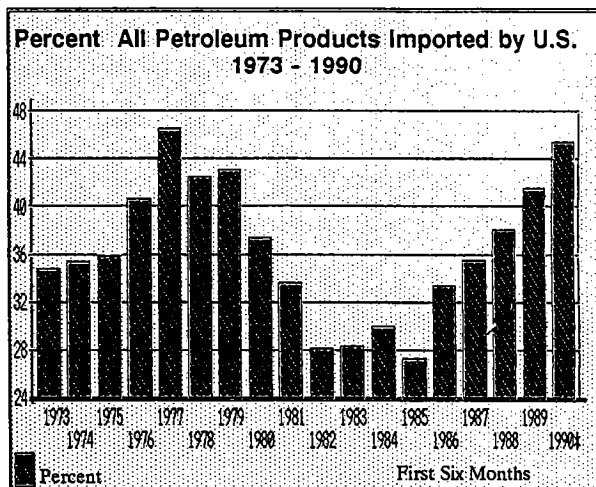
ENGLEWOOD, Colo. (AP) — A financial adviser afraid to face his clients admitted in a videotape message that he lost about \$100 million of investors' money by making risky trades in stock options.

More than 1,000 investors may be affected, according to lawyers. Included are several large retirement funds.

"Words aren't adequate to express my regret and sorrow," said Jim Donahue, head of the Hedged Securities Associates limited partnership, based in the Denver suburb of Englewood. "I feel terrible remorse for the things I've done to you."

H. Alan Dill, attorney for the partnership, said the organization has about \$5.25 million in assets remaining and will seek bankruptcy protection to sort out investor claims.

What's the US/Iraq confrontation really all about? They say that "one picture is worth a thousand words." If so, this picture is worth a large book (chart courtesy of *Commodity Information Systems*, P.O. Box 690652, Houston, TX 77269).



America's dependence on imported petroleum products reached 45.4% during the first 6 months of 1990. The only period in history of greater dependence was 1977 at 46.5 percent.

In an article in the current issue of *World Monitor*, John Templeton, the famous and successful investment genius, states that Japan is sending dozens of its investment advisors here to the US on study programs. In time these men will realize that Japanese stocks cannot stay at 45 times earnings while yielding less than 1%. Therefore, in time, the Japanese stock market will get in line with other markets. Templeton notes that the funds that he manages are now completely out of Japanese stocks. **Russell comment:** if the Nikkei stock average was to get in line with the Dow, it would fall from its current level of around 25,000 down to 5-6,000.

Wow! After a twenty year battle, Gilbert Hyatt, a S. California inventor, received (last month) a patent for the microprocessor (this is the fingernail-sized brain used in computers). Hyatt's invention dates back to 1968, five years before engineers at Texas Instruments and Intel received their own patents. Hyatt could be entitled to tens (possibly hundreds) of millions of dollars in royalty fees.

GOLD: This daily chart (courtesy of *Dunn and Hargitt*) tells an interesting story. Prior to Iraq and Hussein, I saw gold slowly forming a major head-and-shoulders bottom. The horizontal dotted line at the 400 level on the chart (basis the Dec. contract) represented the resistance. As gold pushed up to the 400 level, I expected a decline down to roughly the 385 area. Such a decline would have represented the right shoulder of the developing pattern. From there I would have expected a renewed rally to and then above 400. Anything above 400 would have represented a major upside breakout.

It was not going to happen exactly that way. The Iraqi invasion came, and gold, instead of dropping into a right shoulder, exploded in a panic rise to the 425 level. Then last week, as the war-panic psychology simmered down, gold plunged back below 400, and it now looks to me as though we are forming a right shoulder in gold. In fact, if you blot out the "Hussein explosion" from 400 to 425 and just look at the latest action, what you see is a pattern that resembled a classic head-and-shoulders bottom. If this is true, any new rise in gold above 400 should be the real McCoy.

I want to stress again that the true fundamentals for gold do not include Hussein or the rise in the price of oil. The real fundamentals for gold have to do with US deficits, the out-of-control US budget (aggravated even further by the military buildup), the sinking dollar, and declining world liquidity.

Gold is an insurance policy against Washington politicians' willingness to destroy the dollar. Let me put it another way -- nobody ever lost money betting on the willingness of Washington to chose inflation over balancing the federal budget.



LATE NOTES: The good news is that the market is very oversold (although it has been oversold since early July!). The bad news is that an extended extremely oversold condition is a characteristic of a bear market. Oversold bull markets give way almost immediately to powerful advances.

Is this market ready to advance? This low-volume market is so news-oriented and so in the grip (short-term) of program traders that there is absolutely no way of knowing whether the bear is ready to produce a rally or not. Personally, I'm staying on the sidelines. **Important:** A situation un-noticed by most analysts is that the 200-day moving average of the Dow (now at 2744) has now turned down. The 200-day MA will offer important resistance to any potential advance from here.

NEXT MAILING: September 19